

1 IN THE UNITED STATES DISTRICT COURT
2 FOR THE NORTHERN DISTRICT OF GEORGIA
3 ATLANTA DIVISION

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5
6 CONSUMER FINANCIAL)
PROTECTION BUREAU,)
7 Plaintiff,)
8) Civil Action
-vs-) No. 1:15-CV-0859-RWS
9)
UNIVERSAL DEBT & PAYMENT)
10 SOLUTIONS, LLC, et al.,)
11 Defendants.)

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14 Transcript of the Motions Proceedings
15 Before the Honorable Richard W. Story
16 United States District Court Judge
17 July 30, 2015
18 Atlanta, Georgia

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22 Reported stenographically by:
23 Amanda Lohnaas, RMR, CRR
24 Official Court Reporter
25 United States District Court
 Atlanta, Georgia
 (404) 215-1546

APPEARANCES OF COUNSEL:

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On behalf of Defendant
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On behalf of Defendant
Marcus Brown:

Linda Heary Joseph, Esq.

1 (Thursday, July 30, 2015, 11:00 a.m.)

2 THE COURTROOM DEPUTY: Court calls the case of Consumer
3 Financial Protection Bureau versus Universal Debt & Payment
4 Solutions, et al., Civil Case Number 1:15-CV-859.

5 THE COURT: Good morning. We will proceed first on the
6 request on behalf of Mr. Brown for a modification to the
7 preliminary injunction to allow him access to some income
8 and, Ms. Joseph, I'll hear from you at this time.

9 MS. JOSEPH: Thank you, Your Honor.

10 First of all, I would like to thank the Court for
11 permitting me to file a late reply and for admitting me
12 pro hac and it's nice to be here in Georgia. So thank you.

13 I'd like to begin with a little background, Your Honor,
14 to place what I'm going to say in context.

15 Mr. Brown prevailed upon me to assist him with his
16 motion to modify the injunction because due to the asset
17 freeze necessarily he is without any -- and the business
18 shutdown that necessarily flows from that -- unable to
19 support his family and to retain counsel.

20 My firm is a small women's business enterprise. I do
21 have a background in this sort of subject area. I was a
22 former special assistant to the general counsel of the
23 Federal Trade Commission and I've also done a fair amount of
24 debt collection practices work in the Buffalo area and in
25 Arizona as well and I think that's why he came to me.

1 He borrowed funds to hire me. That was -- and actually,
2 they were very limited. And so I find myself here in a kind
3 of an unusual situation because I need to tell the Court
4 ahead of time that even if successful, now that I've gotten
5 into this and I've seen what the revenues are on the six
6 properties, I really doubt that I will be able to continue
7 because my firm is so small and it will be a huge financial
8 burden. Nonetheless, I do hope that I'm able to assist him
9 at least by way of this motion to help him to get some
10 financial wherewithal to be able to both defend himself in
11 some fashion and to support his family.

12 Before reaching the merits of the motion I'd like to
13 touch upon my concerns here as to the due process issues
14 raised by what I've learned in the short time that I've been
15 in this case, and I really have to emphasize it's a very
16 short time that I've been involved.

17 I think it's important, particularly since I cannot
18 remain in this litigation for the duration, to make the Court
19 aware of several what I consider to be troubling events that
20 I think have occurred here.

21 One of them relates to service of process. I was told
22 by my client that there were threats of contempt unless --
23 and that, you know, there were allegations made that he had
24 been personally served that weren't correct and he agreed
25 then, because he was concerned about contempt of court, to go

1 forward with his deposition and he was actually served by the
2 marshal at the deposition. The deposition was interrupted or
3 this happened beforehand.

4 And I went back and looked at the record because, you
5 know, I wondered about that and I thought, well, maybe there
6 had been an attorney who had accepted service of process in
7 his behalf and I actually found that the only affidavit of
8 service was on May 14th, the day of his deposition.

9 The second thing that I found to be really troubling,
10 and again this goes to the due process issue and, you know,
11 in terms of representation by counsel, related to a couple of
12 things.

13 One was the insistence on the right to the rentals in
14 these properties that I'm going to be speaking about because
15 in my experience in working for the government previously,
16 the information that these properties were purchased long
17 before any of the events that are the allegations of the
18 complaint are publicly available information. I was able to
19 get it fairly quickly and, as you saw, Your Honor, I attached
20 the evidence to the affidavit. So I found that troubling as
21 well.

22 And then the final thing that I found troubling revolves
23 around this issue of the \$9500 attorney fee that I believe my
24 client paid to a lawyer who subsequently had to withdraw due
25 to a conflict. And that that's not been returned.

1 Initially I had understood that the lawyer had kept it
2 because of services that were provided and there was some
3 confusion on this on my part. But I have learned since, and
4 I think now based on conversations with plaintiff's counsel,
5 I believe that this did not occur and that the funds are in
6 fact available and weren't applied to services because of the
7 conflict, there weren't any services delivered.

8 And I understand that the CFPB has taken the place that
9 because this is derived, you know -- in my view this is cash.
10 I've informed the plaintiff's counsel that this is cash from
11 these same properties that was collected as rent. Yes, it
12 was before the issuance of the preliminary injunction, but
13 yet it really has nothing to do with the litigation.

14 And I even thought we might be able to reach an
15 agreement on this. But then I was told that an affidavit
16 setting forth these facts, that this was cash, would only --
17 would not be sufficient because it would be a self-serving
18 affidavit.

19 And I really felt that, you know, my client needs this
20 money to be represented and to have due process honored. And
21 I really was rather shocked at the fact that a sworn
22 affidavit wasn't sufficient. And this is not something
23 addressed in my reply papers because I, as I said, I had
24 originally thought that the money went to the prior attorney,
25 but I have brought along an affidavit from my client which is

1 signed under oath and notarized by me, it was signed in my
2 presence, and it does explain this, that this is cash from
3 these same rental properties.

4 So I'd like to be able to address that as well and, you
5 know, I even wonder if, given what I know about the
6 enforcement programs that the FTC and the CFPB have underway
7 right now across the country, and I know that some of these
8 programs are leading toward criminal prosecution, you know,
9 because these are very serious allegations and whether
10 they're correct or they're wrong, I mean I just do not know
11 the facts here, but I do believe very sincerely, Your Honor,
12 that these defendants are entitled to a defense, particularly
13 if what I believe is going to be in the offing as possible
14 criminal prosecution, that perhaps there should be a public
15 defender status accorded or something done to make sure that
16 these individuals are accorded due process.

17 Having said all of that, I would like to now turn to the
18 substance of my motion, which is really very simple and
19 really involves only two things.

20 And I do -- is it possible for me to hand up to the
21 Court today this affidavit on the \$9500?

22 THE COURT: Yes.

23 MS. JOSEPH: I brought along extra copies for counsel.
24 I'm afraid I don't have too many.

25 It's just a minor point that this affidavit makes, which

1 simply is that the money, the \$9500 that was paid to the
2 attorney came from cash rentals collected from tenants on the
3 same six properties that I'm discussing today. And that I
4 really don't -- I realize that the order as it's written
5 takes a different position with regard to property that
6 predates the injunction and postdates the injunction.

7 And in my view, because this has nothing to do with, or
8 is not tainted, so to speak, that this money should be made
9 available to Mr. Brown, both for defense and/or supporting
10 his family. He has nothing right now.

11 The second point of my argument is with respect to the
12 six properties, and I think the papers are very clear on
13 this. I mean, we showed the documentation that these
14 properties were purchased long before any of the events that
15 are at issue here. We provided copies of the deeds, the
16 dates, and so forth. And so therefore, even under the terms
17 of Your Honor's order, the rent from those properties
18 certainly should be released.

19 It's not going to be a tremendous amount of money after
20 the taxes and the water and all the rest of this. And these
21 properties are on the east side of Buffalo. They are in
22 some -- they are properties that are, shall we say, not the
23 best properties in town. They are difficult properties to
24 maintain. Mr. Brown's a minority person and he is, I
25 believe, doing a service to the community by providing homes

1 to these people.

2 And it's not an easy job. In the winter in Buffalo you
3 have to remove the snow. Previously these were maintained
4 when Mr. Brown was in business; now he's doing this work
5 himself.

6 And I really -- the other thing I learned just
7 yesterday, or I think it was during conversations with
8 opposing counsel, which we tried to resolve this but weren't
9 able to, was that there's a list of properties that relate to
10 the corporate entities. And I really wasn't aware of those.
11 I did a search under Mr. Brown's name to find the six
12 properties that I've put before the Court but I also think
13 that it's possible -- those properties I would presume are,
14 you know, I believe they belong to his sister because these
15 corporations -- the corporation that was involved was, at
16 least one of them was, I know it was his sister's, it wasn't
17 his. They may not be in his name but I suspect given the
18 family relationship that he's going to be doing the
19 maintenance and keeping these properties going.

20 I'm just thinking -- in fact, this occurred to me last
21 night as I was traveling down here -- that maybe we should
22 have been, and maybe I should have been addressing that issue
23 as well. But as I said, I wasn't familiar with those.

24 But I do want to make the Court aware of that, that
25 there is probably rental income there because opposing

1 counsel asked me to obtain documentation with regard to the
2 income and so forth. And that's post-income. And, again,
3 it's on real property; it has nothing to do with debt
4 collection.

5 I understand their position that perhaps the property
6 itself was paid for in some way by proceeds of the debt
7 collection business but I just wanted to make the Court aware
8 of that.

9 And, you know, to me the rental income on the six
10 properties is absolutely clear. I think the \$9500 is
11 absolutely clear. I also think that if he has to maintain
12 and do the work to keep those properties going, I don't think
13 that, with all due deference, that opposing counsel is going
14 to want to come to Buffalo and deal with these properties; I
15 think he should be compensated for it in some fashion if not
16 able to keep the rent, or at least his sister keep the rent.

17 So that's really what I wanted to say to you this
18 morning, Your Honor. Thank you.

19 THE COURT: So essentially at this point what you're
20 asking for is the income from these six properties, that he
21 be permitted to use that income for such purposes as family
22 expenses or attorneys' fees or that that be income that he's
23 entitled to, and you're requesting that the attorneys who
24 were paid the \$9500 be released to turn those funds back over
25 to him?

1 MS. JOSEPH: That's right, Your Honor. And I mentioned
2 the other properties because I think we should keep that
3 issue open. It only came to my attention yesterday when they
4 sent me a chart of those properties. Thank you.

5 THE COURT: I'll hear from plaintiff.

6 MR. DUDLEY: Good morning, Your Honor.

7 THE COURT: Good morning.

8 MR. DUDLEY: As Your Honor is no doubt aware, this case
9 involves very serious allegations of a phantom debt
10 collection scheme.

11 As set out in the complaint, as well as the supporting
12 papers the CFPB filed in support of the temporary restraining
13 order and in support of the preliminary injunction, it's our
14 contention that Mr. Brown and the debt collectors coerced
15 very vulnerable consumers to pay millions of dollars on debts
16 that they did not owe.

17 Now, we've managed to freeze some assets and locate some
18 assets but those assets pale in comparison to the amount that
19 we have identified that was taken from consumers. We
20 estimate over \$3 million was taken from these very vulnerable
21 consumers and we've managed to trace and freeze approximately
22 \$350,000.

23 So it's undisputed that the \$9,500 retainer fee relates
24 to proceeds that Mr. Brown obtained, or the debt collectors,
25 rather, obtained before the issuance of the preliminary

1 injunction. So therefore under the terms of the preliminary
2 injunction it would fall clearly under the asset freeze.

3 Also under the case cited by the CFPB in our response
4 brief, *FTC v. IAB Marketing*, and that's 746 F.3d at 1228, the
5 proper consideration is the amount of consumer harm as
6 compared to the amount of assets frozen. And so here there's
7 a vast disparity between the approximately 350,000 that's
8 frozen and over 3 million in consumer harm.

9 Also, with respect to the \$9,500, it doesn't appear to
10 actually be Mr. Brown's money. Looking at the financial
11 disclosure statements, this would be Document 16 filed for
12 WNY Account Solutions, Universal Debt Solutions, on page 10
13 the \$9,500 retainer fee is listed as cash held by those debt
14 collection entities, not Marcus Brown.

15 So the description is name and address of financial
16 institution, it says Baker Donelson. Account number says
17 retainer and current balance, \$9,500. So that appears on
18 that financial disclosure statement, not on Mr. Brown's
19 personal financial disclosure statement.

20 With respect to the six properties at issue, the Bureau
21 does not object to Mr. Brown receiving rents for those
22 five properties -- for five of the six properties on an
23 ongoing basis going forward.

24 One of the properties is held by his wife, Tasha
25 Pratcher. She has not moved for a modification of the

1 preliminary injunction and we don't believe it's proper for
2 Mr. Brown to take rents for her property, especially when
3 she's represented by separate counsel and recently filed an
4 answer of her own in this matter. If she wants to bring that
5 up, then she can do that through her counsel to us.

6 With respect to those five properties, as I said, the
7 Bureau does not object to Mr. Brown receiving those rents on
8 an ongoing basis going forward. We do, however, wish to
9 reserve the right to potentially seek those rents in arrears
10 and to seek those properties as part of the overall estate
11 used to compensate harmed consumers if we're successful
12 ultimately in our claims.

13 THE COURT: Which is the property that you're excluding
14 from the list?

15 MR. DUDLEY: 237 Dartmouth, Your Honor.

16 THE COURT: Okay, thank you.

17 MR. DUDLEY: Also, with respect to the rents on an
18 ongoing basis, we would request that Your Honor issue an
19 order requiring Mr. Brown to file monthly statements with the
20 Bureau indicating all the rents coming in and also
21 documenting all expenses going out, and also providing
22 verification for those expenses, such as receipts, invoices,
23 bills, things to verify that these are legitimate expenses.

24 In addition we believe that the properties held by WNY
25 Account Solutions and Universal Debt Solutions, there are

1 approximately 15 properties, I believe, held by those two
2 entities, that those remain subject to the asset freeze
3 because those were so intertwined with the debt collection
4 scheme that they can't properly be segregated and would not
5 be subject under the plain language of the preliminary
6 injunction to be lifted.

7 But we would also request that, to the extent there are
8 still expenses coming in and expenses going out for those
9 other properties, that Mr. Brown and the debt collectors
10 provide verification of those amounts and monthly statements
11 for those rents and expenses.

12 THE COURT: How is that being handled now?

13 MR. DUDLEY: We are not aware of how it's being handled,
14 Your Honor. We're not receiving any information about them
15 and it's unclear to us what's happening with those
16 properties.

17 Finally, the other issue I'd like to raise with the
18 Court today is the incomplete nature of the financial
19 disclosure statements that have already been filed.

20 So just to point out a few of the deficiencies, again
21 turning to one of the financial disclosure statements, this
22 one is Document ECF Number 16, so this would be the financial
23 disclosure statement for WNY Account Solutions and Universal
24 Debt Solutions.

25 First of all, this is a joint financial disclosure

1 statement; there should be separate financial disclosure
2 statements for each entity. Also there are just many
3 implausible things about this on its face.

4 So these entities recognized a million dollars in
5 revenue in both 2014 and 2013, but they had no expenses other
6 than a hundred thousand dollars in consulting fees to Marcus
7 Brown and they list no employees. This is just not
8 plausible.

9 During the immediate access to the debt collectors'
10 premises we found a very sophisticated boiler room operation
11 with multiple employees making dunning calls, sending dunning
12 letters. None of that appears in this financial disclosure
13 statement or any of the other financial disclosure
14 statements.

15 Also these financial disclosure statements don't list
16 any related entities. We know that the debt collectors
17 operated a very complex and tangled web of corporate entities
18 and it would be helpful for us to be able to sort that out if
19 they were included in the financial disclosure statements.

20 Similarly, the financial disclosure statement ECF
21 Number 5, so this would be Universal Debt & Payment
22 Solutions, shows 1.2 million in revenues in 2013, and also
23 1.2 million in expenses. So it almost entirely cancels out.
24 The expenses is not just aggregated at all, so we're not able
25 to tell what of that 1.2 million went to wages, to salaries,

1 what went to rent. It's a completely opaque figure and is
2 relatively meaningless as a financial disclosure.

3 So in sum, Your Honor, we would -- we do not oppose Your
4 Honor issuing an order allowing Mr. Brown to collect rents on
5 the properties that belong to real estate of distinction. We
6 would take exception with his collecting rent at 237
7 Dartmouth because that's a property owned by Tasha Pratcher,
8 a separate defendant with separate counsel in this matter.
9 But we would request that Mr. Brown and the debt collection
10 entities provide monthly statements for those properties and
11 for all the other properties held, and also submit new
12 financial disclosure statements that are complete, truthful,
13 and accurate, and allow us a meaningful basis to assess their
14 financial position and trace any remaining assets.

15 THE COURT: Have you conferred with the parties about
16 the financial statements on those that you've just mentioned
17 to me? Has there been contact with counsel stating what you
18 feel are the shortcomings requesting the additional
19 information?

20 MR. DUDLEY: We've had some initial discussions about
21 that, Your Honor. But since Ms. Joseph is relatively,
22 Attorney Joseph is relatively recent to the case we haven't
23 had a chance to go further down that road.

24 And also, sorry, I believe it's Attorney Joseph's
25 position that she only represents Marcus Brown, not the other

1 debt collection entities, so that she doesn't have any
2 authority to make that agreement with us.

3 THE COURT: As far as that goes, obviously my
4 expectation is that the plaintiff would have some
5 communication with any party whose disclosures are not
6 adequate and give them an opportunity and then bring it to
7 the Court, as opposed to -- I'm hesitant to just issue a
8 blanket order that says give them everything they want.
9 There needs to be some discussion and if they're not doing
10 what I've required them to do in this order let me know and
11 then we jump in and take care of it at that point. But until
12 then that would be my expectation, that there at least be an
13 overture, either to counsel or to the party, so that there's
14 an opportunity for them to address that. Okay? Thank you.

15 MR. DUDLEY: Thank you, Your Honor.

16 THE COURT: Ms. Joseph, do you wish to respond?

17 MS. JOSEPH: Yes, I would like to briefly, Your Honor.

18 One thing that I overlooked mentioning was with regard
19 to deposits, this reference to the 9500, we addressed that in
20 our reply papers and we made the point that, yes, there were
21 at times deposits of rent made in to but that was actually,
22 you know, those -- that those funds were actually balanced
23 out. And I still think that because this is cash that came
24 from these rental properties, and given the need for due
25 process here and also for this man to represent his -- you

1 know, to take care of his family, that I think that equity
2 suggests that the \$9500 should be released.

3 As to the five out of six, if Your Honor looks at the
4 deed to Exhibit A, which is that particular -- it's Exhibit A
5 to the affidavit, Marcus Brown is the person who bought it.
6 He transferred the title over to his wife in 2005, and he
7 initially purchased this property.

8 And it is his wife. I mean, to say under these
9 circumstances that they should make a separate application,
10 particularly given the financial circumstances of this
11 family, I think is a bit overreaching and overbearing.

12 As to the incomplete nature of the disclosures, again,
13 there's been pressure placed on me to do this. Yesterday I
14 asked for the disclosures because my client didn't even have
15 the financial disclosures. And plaintiff's counsel directed
16 me to go to someone else to get those documents. They've
17 never been even sent to me or discussed with me.

18 And obviously, you know, there is no indication, as far
19 as I know, of ownership by Mr. Brown of these two companies
20 that they want further disclosures. We're willing to assist
21 in any way but we need to be able to protect his rights. I
22 mean, as I understand it Mr. Bagga owns one of the two
23 companies and was ill and I've explained all of that to
24 opposing counsel.

25 But I really appreciate Your Honor's recognition that

1 this is, you know, a more complex issue that needs to be
2 addressed separately. Thank you.

3 THE COURT: All right. I am going to order that
4 Mr. Brown can receive the rental incomes from five of the six
5 properties. And I appreciate what you're saying about he
6 bought it, but he transferred it to his wife, she's a
7 separate party here. She may want that money; I'm not going
8 to give him her money.

9 MS. JOSEPH: Understood, Your Honor.

10 THE COURT: I quit doing that when I left superior court
11 so I'm not going down that road. So five of the six I will
12 allow, I will provide that he may receive those proceeds.

13 In all honesty, I'm going to require him to keep the
14 Bureau advised of the income. I appreciate why you want to
15 have the expenses but the reality is we're talking about such
16 a small amount of money, if he wants to buy his groceries
17 with it I don't want him to give you the Publix bill. You
18 need to know how much is coming in so that if it changes
19 significantly you folks need to know that. So he will be
20 required to advise you of the income; I'm not going to
21 require him to keep books on the expenses related to that.

22 As to the \$9500, I am extremely sensitive to the fact
23 that the allegations about the losses that were suffered here
24 are astronomical as opposed to what assets you've been able
25 to seize at this point and so I'm very sensitive to that

1 issue.

2 I'm also sensitive to the nature of the allegations and
3 the possible criminal repercussions that can flow from what's
4 alleged here.

5 Under the circumstances and based on what's submitted
6 here, I am inclined to allow him to use that \$9500 to retain
7 counsel. At the same time, it's a little unfair to you folks
8 that you get hit with this without a chance to offer
9 something. If you wish to offer further objection I will
10 give you seven days to offer that in writing to me and I will
11 take it under consideration.

12 So the order on the \$9500 is held in abeyance for seven
13 days so that if the plaintiff wishes to be heard I'll hear
14 their argument on that and not make that ruling final for
15 seven days; but as of today we'll allow him to have the
16 income from this point forward derived from the rental
17 properties.

18 MS. JOSEPH: Thank you, Your Honor.

19 THE COURT: We had also, I think, set down the motions
20 to dismiss that have been filed. Let me preface this by
21 saying I've read your briefs and, quite honestly, I don't
22 want to take a long time with this because I thought the
23 briefs were excellent on both sides and I think draw into
24 focus where the issues lie. I think there are some somewhat
25 novel issues, particularly, I think, where we're plowing new

1 ground, arguably, in terms of the standard concerning whether
2 you're knowingly or recklessly providing substantial
3 assistance and what terms, how that's going to be defined
4 here.

5 So I'm happy to hear whatever you want to say but in a
6 very limited format, but that's where I think that's where my
7 greatest interest lies in terms of where you might offer me
8 something new, having now had the chance to see each other's
9 briefs. So that's an area that I suggest to you but if there
10 are others that you think you would want to highlight for me
11 to make sure I didn't miss it in the reading of the briefs
12 I'm happy to hear that as well.

13 So I'll hear from the movants first and then I'll hear
14 from the plaintiff.

15 MR. BALDRIDGE: Good morning, Your Honor, Doug Baldridge
16 from Venable on behalf of Global Payments.

17 Keeping in mind that we want to keep this rather
18 truncated, as you just stated, I'm going to try to jump right
19 to it. But I do want to thank you for, you know, going with
20 the procedure of allowing us a little oral argument on this
21 because I think as far as a commercial case goes, there's
22 some pretty important things in front of you.

23 The two critical issues that concern me in the context
24 within which we are dealing with this 12(b)(6) motion are
25 that, as you've said, you're going to have to figure out what

1 the legal standard is going to be that we apply to completely
2 legitimate and honest companies like Global Payments, a
3 publicly traded company, and how you're going to hold them
4 responsible, if at all, for the acts of others. A company in
5 this context that has no contact with consumers, which I
6 think is an important part of this.

7 The second thing I think we're going to have to figure
8 out, it's important to me, is to what extent in deciding this
9 standard are you going to allow the CFPB to, in my view, push
10 its regulatory duties and its policing duties on clients like
11 mine that are four times removed from consumers, essentially
12 what we call and what we've said to be making us insurers and
13 guarantors of what merchants do in a sea of literally
14 millions of merchants that are processing hundreds of
15 thousands, if not millions, of transactions every month,
16 every year.

17 So those are the big issues before you and they're the
18 ones that I think justify a little oral argument.

19 Now, what happens when you ultimately decide what the
20 standard is and how we're going to go with this is going to
21 have an impact. Everything you do has some impact,
22 hopefully.

23 And in this situation the Bureau charged with protecting
24 consumers, if we adopt their standard, I can tell you right
25 now that that's going to add enormous cost to what is largely

1 an automated system and those costs are ultimately going to
2 be borne by consumers. That's where it goes because we
3 aren't the ones out there dealing with the consumers. We,
4 Global, are the ones providing that technology platform, that
5 infrastructure, as they've alleged in their complaint, to
6 make this pipeline work to get payment.

7 Moving to the issues, you know who we are, we've been in
8 here before. But to give it a little context, we process 6.5
9 billion in payments a year. We've got 1.5 million merchants.
10 In this case we're talking about two very small merchants,
11 there are six in the case but two that my client processed
12 for, and it is in a sea of other merchants.

13 As I've already said, we are four times removed from the
14 consumer. You've got the consumer at the base level, then
15 you've got the merchants, then you've got our particular way
16 of doing business with independent service organizations,
17 then you've got Global up here at the top, which is
18 performing this automated function of providing the
19 technology platform.

20 There's no dispute about that, the complaint makes it
21 fairly clear that they know we have no consumer or even
22 merchant contact, for that matter.

23 Now, Rule 12(b)(6) and getting to the standards. We
24 moved to dismiss on Count XIII and Count IX. Let's take them
25 in that order.

1 Starting with Count XIII, in summary, as you well know,
2 they allege that Global knowingly or recklessly provided
3 substantial assistance in connection with this phantom debt
4 scheme that the merchants allegedly were involved in. That's
5 paragraph 327 of the complaint.

6 What's before you is what in heck does "recklessness"
7 mean in this context. And everybody agrees on both sides
8 that there is no case law addressing 5536 or 12 U.S.C.
9 5536(a)(3), so we've got to find that guidance somewhere. So
10 where do we go?

11 The way we briefed it, as you know, is we went to what
12 we thought was the most developed area of law, and that was
13 under the Securities and Exchange Act of 1934. And that act
14 says to be reckless the courts, at least in this circuit,
15 have held you've got to plead facts that shows an extreme
16 departure from the standard of ordinary care under
17 circumstances that were so obvious that the defendant must
18 have been aware of the fraud. That's the *Mizzaro Home Depot*
19 case that we've cited in our memo on page 18.

20 Now, we said that's the standard, Judge, that we want
21 you to apply because that's the developed law in this area.

22 What does the CFPB say back? They haven't debated that.
23 What they said is, Oh, that's pre-Dodd-Frank so it's
24 different now, it's different after Dodd-Frank and there is
25 no case post-Dodd-Frank. And they cite the *SEC v. Apple* case

1 and say they didn't decide the issue but they didn't do
2 anything really either way.

3 Well, I would suggest to you if you look in the reply
4 brief, and while certainly not binding on you, the *Subaye*
5 decision out of the Southern District of New York in fact
6 applies the extreme departure standard and the so obvious
7 standard post-Dodd-Frank. We still think it is the most
8 reliable precedent for you to look at in deciding what
9 recklessness means.

10 Now, in this case I believe that if you apply that
11 standard, the ones that we would adopt from the SEC case law,
12 that you are going to find that there is no extreme departure
13 in situations that were so obvious that my client must have
14 been aware that there was ongoing fraud. I think the
15 complaint falls way short of that. It falls way short of
16 that in a number of ways.

17 THE COURT: Let me ask you this. The argument is made
18 that, while you may be correct these are issues that a jury
19 ultimately -- that it's too early to make those decisions at
20 a motion to dismiss, perhaps not at a trial but perhaps at
21 summary judgment with the development of a record that
22 supports the arguments that you make, but at least at the
23 motion to dismiss stage they have alleged that you were
24 reckless and that you had knowledge and that these other
25 events occurred and therefore I shouldn't throw it out at

1 this point; if you're going to prevail it should happen at
2 the summary judgment stage or ultimately at trial.

3 MR. BALDRIDGE: That's an interesting question but it's
4 interesting to me because, having practiced for 30 years,
5 that's what everybody always says when they're defending
6 against a Rule 12(b)(6) motion: Oh, wait for summary
7 judgment, there's more there.

8 Well, let's look at that, though, let's look at what
9 they say in this situation. And I want to direct you to
10 paragraph 328 of the complaint.

11 First of all -- and this is an issue we'll get to
12 separately at the end that I want to bring to your
13 attention -- the allegation is against the payment
14 processors. It's not against Global, it's not about conduct
15 of Global Payments; it's about the payment processors.

16 And I've spoken with each of the payment processors'
17 counsel and I think each of us is more than willing to defend
18 our clients' actions, but we have a right after over a year
19 investigation by the federal government to know specifically
20 what they say we did so we can defend against it. The
21 complaint is deficient in that regard standing alone because
22 it lumps us together.

23 Then 328 says, well, Global, because they're one of the
24 payment processors, enabled merchants to accept debit or
25 credit cards. Well, somewhere four times removed, I suppose

1 there may be some truth to that. Is allowing merchants to
2 accept debit and credit cards even a plausible allegation of
3 an extreme departure so obvious that the fraud must have been
4 known? No, it's not.

5 Two, they say we legitimized the merchants. Well, you
6 know what? If you're a landlord and you give a merchant a
7 building that's going to be there day after day, you've
8 legitimized the merchant. To me, that is not an extreme
9 departure type of allegation, right on the face of the
10 complaint.

11 We make transactions easy. So does cash. Cash makes
12 transactions easy. It's not an extreme departure.

13 And we enabled merchants to accept payments from
14 consumers. That's what we do. We don't deny that somewhere
15 in this long chain of people that's exactly what we do. But
16 none of this comes even close to establishing an extreme
17 departure from the standard of ordinary care.

18 Now, this leads us, though, into the second question
19 you're asking, and that's really the Rule 9(b) stuff. And
20 it's an interesting thing because I'm sure you're well aware
21 in the *Hanna* decision your fellow judge Totenberg had looked
22 at the issue and said that Rule 9(b) doesn't really apply
23 here.

24 There's two problems with what she did and why I would
25 encourage you to look at this a little differently. And the

1 first one is really not a problem.

2 If you go to pages 53 and 54 of her opinion, she
3 analyzes the situations in which Rule 9(b) apply and it's
4 basically about protecting reputations when fraud allegations
5 are made such that a party should be entitled to more clarity
6 as to what they allegedly did.

7 But in the *Hanna* decision Judge Totenberg did not have a
8 situation where there were allegations right on the face of
9 the complaint of fraud. She had the situation where there
10 was what I would call a mortgage foreclosure mill that wasn't
11 really disclosing that they were not looking behind the
12 content of affidavits or perhaps lawyers were not pursuing
13 it, and she said that's not a fraud situation and that
14 doesn't meet the eight-part standard of *Wright & Miller* for
15 deciding whether Rule 9(b) should apply, which is on -- in
16 her opinion.

17 The second point I would say is then she leaps and she
18 says -- and this is where I think it was a problem -- that
19 there's been no circuit that's actually applied Rule 9(b) in
20 the Consumer Protection Act scenario.

21 Well, respectfully to the judge, she's just wrong.
22 *Kearns v. Ford Motor*, 567 F.3d 1120, in the very
23 consumer-friendly Ninth Circuit in 2009, applied Rule 9(b)
24 standard, admittedly to a state Consumer Protection Act
25 situation. And then you also have *Spaulding v. Wells Fargo*,

1 714 F.3d 769, Fourth Circuit, 2013, that does the same.

2 Those cases weren't briefed.

3 Now, what I wanted to tell you here is it's not all
4 about the particularity like we often see in fraud cases, the
5 who, what, when, and where. To me, as we cut through all the
6 briefing and the lawyers going back and forth, it really
7 boils down to lumping. You've got a lot of people in this
8 tent, including some people that are pretty far removed from
9 the actual conduct, including my fellow, the ISOs and us.

10 What is it that they think we did? Rather than putting
11 us all three together, we have a right to respond and say
12 what facts do you have? What plausible allegations can you
13 make against us under *Iqbal* and *Twombly* such that we can
14 defend, rather than just generally saying you legitimized
15 these guys, you have a right to see chargebacks, without even
16 explaining what chargeback we saw and rejected.

17 You have policies. Well, what policy did we violate?
18 You know, we have a right to know that.

19 So taking *Hanna*, both acknowledging that *Hanna* was not a
20 fraud case and that truly the couple of cases were missed in
21 making that broad, sweeping statement, I think at a minimum
22 they've got to replead under 9(b) and let us know what we did
23 and delump, if you will, or unlump the various payment
24 processors.

25 Now, quickly getting to substantial assistance, which is

1 a second part of the 5536 claim, what is substantial
2 assistance? Well, it really means there's got to be a
3 substantial link between the assister, if you will, and the
4 resulting harm. Whether or not proximate cause is required,
5 nobody seems to know; it goes back and forth.

6 Now, what we do know, though, is if we apply the *Apuzzo*
7 decision, again borrowing from the SEC case law, that one
8 element of what constitutes substantial assistance is grossly
9 missing from the pleading in this case, and that is that the
10 assister must participate in something that it wished to
11 bring about. That it wished to bring about, that's pages 212
12 and 213 of *Apuzzo*.

13 No one is ever going to allege that Global Payments
14 intended to bring about what allegedly happened to these
15 consumers as a result of the conduct of the merchants. That
16 in and of itself, if you adopt the SEC standards, means
17 substantial assistance has not been alleged.

18 What does the CFPB say back? Well, he says, well, these
19 folks -- lumping them all together again -- they played a key
20 role. That's what they say, they say they played a key role,
21 and that's on page 14 of the opposition.

22 Well, there's no such thing as the key role standard and
23 they're certainly not -- that's certainly not alleged in the
24 complaint itself, which is what you have to focus on as
25 opposed to what they say in the briefs.

1 So for those two reasons, taking the 5536, the bottom
2 line is if you apply the SEC case law the pleading fails; it
3 does not plead sufficiently what we did. You add to it
4 Rule 9(b), it lumps us together so we don't know what we did
5 in a situation where fraud is definitely alleged, unlike in
6 the *Hanna* case.

7 Very quickly on unfair acts and practices, which is
8 Count IX, the whole issue here really boils down to did we
9 inflict some substantial consumer injury.

10 Now, you have to decide whether there's plausible
11 allegations with this many links between the consumer and
12 Global Payments, performing a largely automated process,
13 whether there's sufficient allegations of substantial
14 consumer injury caused by our conduct.

15 I would suggest that when you're four parties removed,
16 when you're providing an automated technology platform, when
17 there's no evidence whatsoever, or even an allegation, I
18 should say, that we knew of the fraud, I really don't know
19 how you could establish substantial consumer injury that
20 remote on the face of this pleading.

21 Do you have any questions?

22 THE COURT: No, sir. Thank you.

23 MR. BALDRIDGE: Thank you very much for your time.

24 THE COURT: All right. Let me hear from the plaintiff
25 and then I'll do the other defendants and we'll move it that

1 way so that you can directly address the issues raised.

2 MR. ENGEL: Thank you, Your Honor. Good morning,
3 Jonathan Engel on behalf of the Bureau, Your Honor.

4 In April, as you know, this Court found that the
5 Consumer Financial Protection Bureau is likely to succeed on
6 the merits of its claims against certain individuals and
7 entities for their role in a phantom debt collection scheme.

8 And we alleged that these debt collectors took millions
9 of dollars from consumers, money to which they had no
10 legitimate claim, based on threats they used to obtain
11 authority or without obtaining consumers' authority at all.
12 They were able to access these consumers' bank accounts
13 because they had the help of Frontline, Pathfinder, and
14 Global.

15 I want to touch on the unfairness piece just because
16 that's that what was left lingering first and then, of
17 course, I'll address their concerns with regard to
18 substantial assistance.

19 We've alleged that Frontline, Pathfinder, and Global
20 each knew of the risk of processing for debt collectors.
21 These debt collectors fell into three categories that
22 required heightened scrutiny: A, they were debt collectors;
23 B, they were aggregators; and, C, they were card-not-present
24 merchants.

25 Despite falling into each of these three categories,

1 Frontline, Pathfinder, and Global ignored their policies and
2 procedures at the underwriting stage and at the monitoring
3 stage and allowed them entry into the payment processing
4 system and then allowed them to access consumers' bank
5 accounts.

6 And their failure, Frontline, Pathfinder, and Global's
7 failure to adequately or meaningful underwrite and monitor
8 these accounts amounts to an unfair act and we also allege
9 that it substantially assisted the debt collectors' primary
10 violations.

11 THE COURT: Let me ask you, because you have put
12 Frontline, Pathfinder, and Global together in your discussion
13 here, and as counsel pointed out, that lumping gives him
14 pause, and I know from their briefing they suggest that there
15 should be a very clear demarcation between them and those two
16 entities, that you've gone another step up the chain, I
17 guess, when you get to them and they have, as I recall from
18 their briefing, there were things in place that caused them
19 to believe Frontline and Pathfinder would provide some
20 protection for them from crossing over lines. And so you've
21 said they knew they were dealing with debt collectors and so
22 forth.

23 While you've alleged that, you've alleged against the
24 group and the suggestion is made if you broke it out into the
25 individual defendants, I hear Global arguing you couldn't

1 allege that as to us legitimately. How would you respond to
2 that?

3 MR. ENGEL: So we have broken out with respect -- and
4 the count indeed does group the payment processors together.
5 But the body of the complaint, the substance of the
6 allegations, breaks out each, Frontline, Pathfinder, and
7 Global, and sets forth their particular role in the scheme.
8 And I can go through if you would like just to highlight a
9 couple of the paragraphs or the facts that we've alleged that
10 we believe establishes that Global had actual knowledge and
11 we can infer that Frontline and Pathfinder had actual
12 knowledge as well.

13 Most importantly, Your Honor, Global possessed and
14 had -- and we allege processed -- and had a duty to
15 investigate chargeback complaints. And we set forth in our
16 complaint a handful of those allegations and those -- rather,
17 those complaints. And those complaints are sworn affidavits
18 from consumers that describe a fraudulent scheme in great
19 detail and in great consistency and in a very similar fashion
20 to which it's alleged in our complaint.

21 So we've also alleged that Global had -- in effect the
22 ISOs had a duty to identify fraud and investigate consumer
23 chargebacks.

24 So Global either fulfilled that duty, investigated these
25 chargebacks, and recognized that there was fraud; or they

1 fulfilled -- or they didn't fulfill that duty and
2 demonstrated an extreme departure from the ordinary standard
3 of care and were therefore extremely reckless. And I'll get
4 to the recklessness piece in a minute. But we have
5 sufficiently alleged, we believe, that they had actual
6 knowledge or at least extreme recklessness.

7 With respect to Frontline and Pathfinder, this Court can
8 infer from atypical business transactions that an entity had
9 actual knowledge or was extremely reckless. And we allege
10 that the departures from the underwriting standard by
11 Frontline and Pathfinder, and indeed by Global as well, show
12 an extreme departure from a standard of care.

13 Each of these entities, Frontline, Pathfinder, and
14 Global, recognized the extreme risk that they were
15 undertaking here and each of them ignored those policies and
16 procedures or consciously avoided the knowledge that was
17 acquired when they did follow those procedures, and that
18 demonstrates extreme recklessness and knowledge.

19 And that's just at the underwriting stage. At the
20 monitoring stage -- now, Global says in its brief that it was
21 the ISOs and not Global that were closest to and ultimately
22 responsible for the behavior of the merchants, including
23 these debt collector merchants. Frontline says it was
24 Global, not Frontline, that undertook a duty to provide
25 ongoing credit review and to handle chargebacks.

1 The Bureau has alleged that Pathfinder and Global
2 identified that Universal, for example, was processing
3 payments for another debt collector. Global notified
4 Pathfinder that various card networks were terminating these
5 merchants, yet Global and Pathfinder continued to process
6 payments for those merchants.

7 We've alleged that Pathfinder received an industry fraud
8 alert. We've also alleged that Global and Frontline were
9 required to consult that same network that provided the alert
10 and therefore we could infer that they had the same
11 knowledge.

12 We've alleged that Global and Pathfinder ignored high
13 chargeback rates that by their own admission signaled
14 suspicious activity.

15 But, again, most importantly, we allege that Global
16 possessed these consumer complaints that described this
17 fraudulent scheme which Global had a duty to investigate and
18 either investigated and identified the fraud and ignored it,
19 or they didn't fulfill their duty to investigate and
20 demonstrated an extreme departure from the standard of
21 ordinary care.

22 I want to address more directly your questions about
23 substantial assistance and the appropriate standard here.
24 And as I said, we believe that we have satisfactorily alleged
25 knowing or extreme recklessness.

1 But we also argue that that is not the appropriate
2 standard here. The Dodd-Frank Act specifically uses the term
3 "recklessness." And we have to presume that Congress knew
4 the content of existing law and where they know how to say
5 something but choose not to, their silence is controlling.
6 They could have very easily said "severely reckless"; they
7 chose the term "recklessness" and that is the term that
8 controls or should control this Court's interpretation of the
9 statute.

10 We clearly satisfy the recklessness standard. And the
11 conventional understanding of recklessness is a known risk of
12 harm and a precaution -- and the precaution that would
13 eliminate the risk involves a slight burden relative to the
14 risk such that failure to adopt that precaution demonstrates
15 an indifference from the risk. And that at least is what we
16 have here.

17 Again, these debt collectors were subject to a
18 heightened or a -- a heightened level of scrutiny all along
19 the way by Frontline, Pathfinder, and Global; yet, they were
20 allowed to access, they were allowed through the gateway into
21 the payment processing network and they were allowed to stick
22 their hands into consumers' bank accounts, which is
23 effectively what happened here.

24 We've alleged certain instances where consumers
25 expressly denied authorizing the debt collectors access to

1 their accounts, and certainly in those instances these debt
2 collectors couldn't have taken money from consumers absent
3 the substantial assistance of these payment processors.

4 And Global seems to confuse the three prongs, if you
5 will, of the substantial assistance standard. We have that
6 it's unlawful for a person to knowingly or recklessly provide
7 substantial assistance, so we have to have a primary
8 violation. And this Court has already found the likelihood
9 of success on the merits of the primary violation. There
10 seems to be no dispute about that piece, at least for our
11 purposes here today.

12 The second piece is the knowing or reckless piece. And
13 as I've said, we believe we satisfactorily met the pleading
14 standard for each of those pieces.

15 And Global says that the fact that we enabled merchants
16 demonstrate -- doesn't demonstrate an extreme departure from
17 a standard of care, but that isn't what we've alleged. We've
18 alleged that they had knowledge and that they're enabling
19 merchants to access consumers' bank accounts and that's
20 substantial assistance. So we have to look at their
21 knowledge and their assistance separately.

22 And with respect to the application of *Apuzzo*, which
23 seems to be the standard, it's a case that all parties have
24 cited and it's certainly relevant to the questions before the
25 Court today, but it's, of course, a Second Circuit case that

1 applies a standard to securities fraud that predates the
2 amendment of the Dodd-Frank Act. So it's of minimal
3 controlling value. With that said, we agree that it is
4 relevant.

5 We also maintain that we've met the three-prong
6 substantial assistance standard set forth in *Apuzzo*, that is
7 that Frontline, Pathfinder, and Global in some sort
8 associated themselves with a venture and they did that by
9 taking on these merchants as clients and to do that they
10 ignored their own underwriting standards, again to take on
11 these merchants as clients.

12 They also participated in this -- in the transaction as
13 something they wished to bring about. And we don't suggest
14 that a big company, a big legitimate company like Global
15 intended consumer harm here. But we do allege that Global,
16 Frontline, and Pathfinder wished for these debt collectors to
17 be successful clients of theirs. They wanted these merchants
18 to succeed and they were indifferent to the fact that that
19 success may harm consumers.

20 They ignored signs and categorized merchants in a way
21 that would allow them access to the system, where if they had
22 followed their own policies and procedures that would not
23 have happened. They sent them gift baskets. They allowed
24 them to continue processing despite red flags all along the
25 way that they were facilitating suspicious activity.

1 But the *Apuzzo* standard does not control and the reason
2 that it doesn't control is that it applies a criminal
3 liability standard that requires a level of specific intent
4 that is incongruent with a substantial assistance
5 recklessness standard. One cannot recklessly wish to assist
6 a fraud.

7 Recklessness, again, is the term that Congress chose to
8 use and the courts that have applied a severe reckless
9 standard have applied it as a substitute for knowledge, not
10 as a substitute for reckless. No court has yet applied
11 recklessness. No court has applied any substantial
12 assistance law under Dodd-Frank -- or rather the CFPA, but
13 under the Exchange Act or the CFPA no court has applied a
14 recklessness standard and discussed whether mere or simple
15 recklessness suffices to establish substantial assistance.
16 So we don't believe that standard applies here.

17 With respect to the 9(b) pleading standard, I want to
18 note that even under a 9(b) standard, knowledge may be there
19 generally and we feel like we've exceeded that standard.

20 I also note that while Global argues that we haven't
21 identified the chargebacks and the policies that were
22 violated, to the contrary, we've specifically identified
23 chargebacks and in fact quoted those chargebacks in the
24 complaint and we specifically identified policies, namely the
25 policy to investigate chargebacks. Those are the facts that

1 we specifically alleged, among others, that satisfy the 9(b)
2 pleading standard.

3 THE COURT: Is it your view that the 9(b) standard is
4 the proper standard to apply to the fraud claim?

5 MR. ENGEL: It is not, Your Honor. We think that the
6 reasoning in the *Hanna* court, among other courts that have
7 applied the CFPA, because this is a Consumer Protection Act,
8 which is not securities fraud we're talking about here, our
9 goal here is to protect the least sophisticated consumer, not
10 the reasonable investor, and for those reasons, along with
11 those cited by *Hanna*, we believe that 9(b) is not the proper
12 standard. Nonetheless, we do believe that we've met that
13 9(b) standard.

14 THE COURT: Okay.

15 MR. ENGEL: If the Court has no further questions let me
16 just say in closing that it is our position that Frontline,
17 Pathfinder, and Global each knew the risk of taking on these
18 debt collector clients and they now seek impunity, despite
19 the fact that this foreseeable risk has resulted in
20 foreseeable harm for thousands of consumers. And for that
21 reason we ask that you deny the motions, Your Honor.

22 THE COURT: Thank you. I'll give you about three
23 minutes.

24 MR. BALDRIDGE: Very briefly, Your Honor.

25 I was confused because counsel encouraged you to not

1 consider *Apuzzo* out of the Second Circuit, but *Apuzzo* is the
2 standard they cited in their TRO proceedings that he started
3 his presentation with. So I think it's pretty clear that the
4 parties, when it serves their interest, like the *Apuzzo*
5 decision. And incidentally, that TRO, of course, has no
6 impact on Global. We weren't subject to that; the Court made
7 no findings about Global.

8 Getting to the Rule 9(b) issue very quickly, counsel
9 told you that, well, when you get to the body of the
10 complaint we give you specifics, and he mentioned some of the
11 things he said.

12 Well, if you start on page 26, even the title lumps the
13 payment processors together. Almost every paragraph starts
14 with "The payment processors did this" or "The payment
15 processors did that."

16 Then you get to 151, which is the most important
17 paragraph of this section, quote: "By granting access by the
18 debt collectors and other persons who collect debt to this
19 payment processing infrastructure, the payment processors
20 enabled them to quickly, conveniently, and efficiently
21 collect consumer payments."

22 Well, what do we do? They're clearly lumped all the way
23 through this pleading.

24 And then when you get to the issue of approval of
25 applications, again they lump the payment processors

1 together, saying certain applications were approved through
2 these merchants with whom we do not have a commercial
3 relationship. And I would like to know if they can even
4 identify one that we approved. That's 164, if you look at
5 paragraph 164: "Although the payment processors classify the
6 debt collectors as high risk, the payment processors approve
7 debt collectors' numerous applications." Name one.

8 This is a Rule 9(b) issue, they are saying we are part
9 of a phantom debt collection fraud situation.

10 Okay. Counsel started out that we knew the risk of
11 processing for the debt collectors. Well, there's no
12 allegation that we knew who the merchants were. There's no
13 allegation that we knew there was a fraudulent scheme. In
14 fact, counsel already said we didn't intend to bring about
15 this harm. That's right, we're four times removed from it
16 and we're providing this infrastructure.

17 Chargebacks, very carefully, there's got to be plausible
18 allegations about the chargebacks.

19 Duty to investigate a chargeback. A chargeback when it
20 comes, and we send down the pipeline to the merchant, if the
21 merchant doesn't contest that chargeback there's nothing to
22 investigate. Our duty is not to investigate fraud; our duty
23 is to make sure the consumer gets their money back through
24 the pipeline.

25 These merchants never challenged a chargeback. There's

1 no allegation that a chargeback was ever challenged. So the
2 duty to investigate, it is not our job to become the CFPB and
3 do their job for them. No consumer lost in the situation of
4 a chargeback because the merchants, for whatever reason, were
5 smart enough not to challenge those when they came back down
6 the line.

7 So in closing, we would really like to know what it is
8 they think we did. We think Rule 9(b) does apply and we
9 think after a year and a half of spending taxpayers' money to
10 investigate this thing that we ought to get a complaint that
11 says Global did this, Frontline did this, Pathfinder did
12 this, so we can figure out what the allegations are. Thank
13 you.

14 THE COURT: Certainly to the extent they apply to your
15 argument I'll allow you to adopt, you don't have to replot
16 ground, I'll allow you to adopt any arguments that have been
17 made, but I'll hear from you in addition.

18 MS. KANSKI: Thank you, Your Honor. Kirstin Kanski on
19 behalf of Frontline Processing.

20 As you know, Frontline is one of the independent sales
21 organizations along with Pathfinder, and therefore I intend
22 to just limit my remarks to the ISOs because it is a
23 significant distinguishment.

24 And I agree with everything Mr. Baldridge said on behalf
25 of Global. One of the fatal flaws, if not the fatal flaw, to

1 the way the CFPB chose to plead its claims was its complete
2 disregard of the various roles of Global and its ISOs.

3 And I'll direct the Court's attention to paragraph 84 of
4 the complaint where the CFPB acknowledges that with respect
5 to Frontline, my client, an ISO, under its MSA with Global,
6 Frontline agreed to market services and prescreen merchants
7 for compliance. And that's it.

8 Otherwise, Your Honor, with respect to the rest of the
9 complaint and the allegations there are no specific
10 allegations that would have put Frontline on notice of any of
11 the fraudulent activity. At most, at the absolute most with
12 respect to Frontline, paragraphs 196 to 218, detail two
13 merchant applications that are in the record that Frontline
14 received prescreened and forwarded on.

15 There is no allegation that would put Frontline on
16 notice of fraudulent conduct or any wide-reaching phantom
17 debt operation at the time it received those applications.

18 I also want to specifically call the Court's attention
19 to the difference in time because Global and Pathfinder were
20 operating with these merchants for more than two years before
21 Frontline even came into the picture. So that might be one
22 plausible reason why there's simply no specific factual
23 reference of any indication of fraud that Frontline could
24 possibly have been on notice of.

25 I also want to just specifically highlight a few

1 critical distinctions with respect to my client, Frontline,
2 as an ISO. Its relationship is only with Global. The
3 services it provided were to Global pursuant to a contract.
4 It was marketing Global's payment processing services to
5 merchants, to commercial entities.

6 There is no connection to consumers directly. And if
7 Global is four times removed from the actual consumers and
8 the payment processing and the consumer transactions, the
9 ISOs, as sales representatives of Global, are just as much,
10 if not more removed from the actual consumer transactions
11 themselves.

12 And with respect to violations of policy, because the
13 CFPB keeps coming back to this point, I want to be sure the
14 Court is clear, because the record and the complaint is,
15 Frontline did not violate any policy because Frontline --
16 debt collection was never a prohibited practice for Frontline
17 and the CFPB acknowledges as much. So there's no allegation
18 that Frontline violated any policy with respect to its own
19 underwriting or Global's.

20 With respect to the chargeback process, that process was
21 handled entirely and its alleged entirely to be within
22 Global, the payment processing transactions are by Global.
23 And, again, Frontline, as simply a sales representative of
24 Global, is outside of that process entirely.

25 So to the extent counsel for the CFPB has emphasized the

1 scant facts it has come up with that would put any of these
2 three parties on notice of any fraud, Frontline is outside of
3 that box entirely.

4 With respect to the distinctions between Pathfinder and
5 Frontline's MSAs, we've extensively briefed those so I don't
6 plan to spend much time on those at all today. But the two
7 main distinctions was, number one, Frontline has no
8 contractual obligation to monitor. Under the Frontline MSA
9 that was not Frontline's role, that was not Frontline's
10 obligation.

11 And with a substantial -- with respect to the 530 --
12 5336 claim and substantial assistance, I think that a
13 critical point, Your Honor, is that the statute plainly reads
14 "knowingly or recklessness provides substantial assistance in
15 violation of 5531."

16 The *Apuzzo* case in the Second Circuit standard and Judge
17 Hand's standard are the most applicable.

18 And when the Court looks to the actual fraud that is
19 alleged to have occurred here, it is detailed at 94 to 143 of
20 the complaint, the actual fraudulent conduct by the debt
21 collectors that is alleged has nothing to do with the
22 submission of the application to be approved by Global or
23 Frontline to be able to participate in the system. So there
24 is simply no pleaded connection by Frontline with the
25 involvement of any of the underlying fraud.

1 And lastly, with respect to the unfair practices, Your
2 Honor, again, telling in the CFPB's opposition paper, we have
3 detailed to the Court why the ISOs are not covered persons or
4 service providers. The only response is this phrase we
5 "played a key role in the network."

6 Well, that falls fall short, doesn't even come close to
7 meeting the statutory criteria to be subject to liability.

8 And with respect to an unfair practice committed by
9 Frontline, I would just join in the arguments that
10 Mr. Baldridge has eloquently stated.

11 And unless there's further questions with respect to
12 Frontline or the ISOs --

13 THE COURT: Thank you.

14 MS. KANSKI: Okay, thank you.

15 MR. BALDRIDGE: I believe I left some paper behind.

16 THE COURT: Do you want to respond now or do you want to
17 wait?

18 MR. ENGEL: I think it would be easier if I just wait.

19 THE COURT: Okay.

20 MR. SMITH: Good morning, Your Honor, John Smith on
21 behalf of Pathfinder.

22 Your Honor, I think it makes sense to maybe start with a
23 little bit of an understanding of what actually happened and
24 I think my colleagues have provided a good analysis of some
25 of the legal standards and requirements that apply, but I

1 think it's important that maybe the Court understand a little
2 bit about what actually happens on the street in real life
3 with these transactions.

4 First of all, the complaint at two defines, the second
5 page, defines Global, Pathfinder, and Frontline, and calls
6 them payment processors.

7 I submit to the Court that there is only one payment
8 processor in the room right now and that's Global.

9 Pathfinder does not process payments for anybody. Pathfinder
10 does not process anything.

11 Pathfinder is an ISO, which is an independent sales
12 organization, that currently has eight employees full time.
13 The ISO has an agreement and a contract with Global and that
14 agreement provides that the ISO, in this instance Pathfinder,
15 will market Global's merchant processing services. So
16 Pathfinder will market the services of the payment processor;
17 it's not actually a payment processor.

18 Pathfinder then often has independent sales agents, a
19 step below Pathfinder. So Pathfinder works through
20 independent sales agent to go out and find merchants that
21 might need the assistance of running a credit card, for
22 example.

23 The sales agents then identify merchants. So Your Honor
24 may think that the sales agent could see a new flower shop
25 that opens, think that that flower shop may want to take

1 credit cards, knock on the door, go in and see if that's
2 something they would like to do; and, if it is, then the
3 individual sales agent will then have paperwork that gets
4 filled out by the potential merchant. That paperwork is then
5 given back to Pathfinder. Pathfinder does some checks.

6 And I think it's important when the Court hears the CFPB
7 talk about these duties, these duties, we need to know where
8 they're coming from. They have a duty to do this and a duty
9 to do that. Where is that duty coming from? Is it coming
10 from a statute? Is it coming from the case law? Where is
11 it?

12 Well, I can tell the Court that with respect to
13 Pathfinder and Global, there is a contract. So we can point
14 to that, at least, for what the obligation is. And what does
15 Pathfinder do?

16 Well, Pathfinder prescreens and underwrites for credit
17 purposes for Global's benefit. So the merchant fills out the
18 paperwork and Global prescreens that and underwrites it for
19 the benefit of Global.

20 So what are the types of things that Pathfinder looks at
21 with a company of eight employees? Well, they look to make
22 sure that the merchant has a business license, for example.
23 So in this instance, the state of Georgia would have issued a
24 business license for a flower shop and Pathfinder would rely
25 on the fact that there's a business license issued for this

1 flower shop in this example.

2 They also want to make sure that the flower shop would
3 have a business account. So they'd get some submission that
4 shows we have a bank account and it's in the name of the
5 flower shop.

6 They'd want to make sure that if they described it as a
7 flower shop on the application, that the thing is indeed a
8 flower shop and not selling doughnuts. So they check and
9 make sure, okay, it is in fact a flower shop.

10 Then they may do a background check on some of the
11 individuals and they're basically determining
12 creditworthiness.

13 They're not a regulatory body. They're not going in to
14 the flower shop to determine if when they sell roses they're
15 really selling tulips. They don't have that power and they
16 don't have that capacity; they can't do that. They can look
17 at the documents and the materials that I just identified and
18 at that point if Pathfinder determines, okay, well, they have
19 a business license, they have a business bank account, it
20 says flower shop, it is a flower shop, and you've looked at
21 their transaction volume, we think we're going to go ahead
22 and recommend that to Global.

23 And that's the other piece of it, Your Honor.
24 Pathfinder doesn't set this in stone. Pathfinder then
25 submits the package to Global. And if Global accepts it --

1 for which Global has the right solely in its discretion to
2 reject any merchant that Pathfinder would provide. Well,
3 Global can look at the application, and in this instance of
4 the flower shop we talked about, but in this instance what
5 we're here about today, they would see that it is a debt
6 collector and they would see all the details that were laid
7 out in the application and then Global would evaluate that.

8 And if Global looks at that and decides, you know what,
9 I think we're going to accept this as a merchant, so
10 according to the merchant services agreement between
11 Pathfinder and Global, if Global accepts that it becomes a
12 merchant.

13 So, again, when we're looking at duties, we're looking
14 at duties flowing from statutes and from law and maybe from
15 contracts.

16 Well, so far we've identified one contract and that's
17 the merchant services agreement between Global and
18 Pathfinder. Well, if Global reviews it and decides, you know
19 what, we're going to accept it, Global enters into a contract
20 directly with the merchant. That contract does not involve
21 Pathfinder or any of the ISOs. Pathfinder is not a party to
22 the agreement.

23 So in this instance, if Global accepted the flower shop,
24 Global would have a new contract and that contract would be
25 between Global and the flower shop.

1 So at that point the ISO, the independent sales
2 organization, has completed the front end of its
3 responsibilities. It had a sales agent go out, knock on the
4 door of a prospective business, determine that they may need
5 some credit card processing, ask them to fill out an
6 application, did some checks that an eight-employee company
7 could do, such as looking and making sure they have a
8 business license and they have bank accounts, provided that
9 to Global, which is the, you know, the -- processes 400
10 billion transactions worldwide and has all the
11 infrastructure. Global approves it; Global enters into a
12 transaction with the merchant.

13 The merchant then, when customers come and present their
14 credit card or they call them with a credit card number, the
15 merchant then swipes that number through some portal and then
16 that information and data gets sent directly to Global.

17 Pathfinder was an independent sales organization; it
18 sold the product. And now when -- the point of sale, credit
19 cards come in, all that goes directly to Global. So this is
20 all between Global and the merchant.

21 Now, Pathfinder's done its job. It did the
22 underwriting, it provided it, it got approved, and then
23 Pathfinder will make a fee off of the transactions generated.
24 And Pathfinder, of course, has to pay a commission to the
25 sales agent that knocked on the door of the flower shop and

1 then Pathfinder gets to keep a little bit more and then
2 Global keeps the rest and that's how the actual transactions
3 work.

4 In this instance Pathfinder, other than the front-end
5 obligation, Pathfinder had an obligation to monitor the
6 merchant process. So Pathfinder had, as between Pathfinder
7 and Global, there was a separate relationship defined in that
8 same agreement, the merchant services agreement. So
9 Pathfinder had in the merchant services agreement a duty to
10 Global to monitor merchant processing activity to detect
11 fraud and risk issues.

12 Well, what was it looking at? Well, Pathfinder doesn't
13 have Global's infrastructure. The transactions aren't going
14 anywhere with Pathfinder; the transactions are going between
15 the merchant and Global.

16 Well, Pathfinder has limited access to Global's systems
17 for the purposes of looking at certain things. Like, for,
18 example, chargebacks. And if there was a, you know, a huge
19 amount of chargebacks there are certain lists that the
20 merchant could get placed on, because, as the Court can
21 understand and is seen in the briefing, if you have 1 percent
22 or 2 percent of chargebacks over time with thousands of
23 transactions and suddenly you only have ten transactions and
24 two chargebacks, you go, oh, my gosh, it's 20 percent, you
25 guys should have gone out and investigated the flower shop.

1 Well, that's because there was ten transactions, not
2 thousands, and that's why the banks, Visa and Master Card,
3 they have certain different rules and requirements that could
4 get people put on lists if there's problems.

5 So Global and Pathfinder at that point, Pathfinder would
6 look and if they see something that's unusual they would
7 either bring it to Global's attention or take steps to do
8 something about it, because if there are chargebacks that
9 don't get paid, in this relationship Pathfinder's obligated.

10 So what is Pathfinder doing? It's assessing the credit
11 risk up front and making sure then that it sends up an
12 application that's completed for Global to approve. And then
13 as the processing goes on, with Pathfinder's limited access
14 to Global's systems, it can actually look and see if there's
15 chargebacks and other things that might cause concern or
16 other reporting agencies, and then if it's so let them know.

17 And Pathfinder has an interest in doing that because if
18 there are chargebacks that aren't paid they're going to be
19 liable for it at the end and they have to pay for it. That's
20 it.

21 So with that obligation of this eight-person company and
22 one contract, which is a contract between Global and
23 Pathfinder, and then Pathfinder's independent sales folks
24 that have gone out knocking on doors, the agreement between
25 the merchant and Global, and then Pathfinder's limited

1 obligation to Global to follow up and see if there were any
2 issues that could cause credit problems, the CFPB would seek
3 to take that agreement between Pathfinder and Global and
4 impose on Pathfinder a superregulatory obligation to
5 investigate and root out fraud at the merchant level.

6 So I would submit to the Court that if this was the
7 flower shop, if the flower shop was selling flowers that it
8 represented were from some country but they were from
9 another, how would Pathfinder know that?

10 And if customers started returning some of those
11 flowers, but as Mr. Baldridge pointed out, the merchant
12 returned the money, how would it know if anything was a
13 problem?

14 So it really causes one to think that if in fact
15 Pathfinder had a duty to go and find out what was going on in
16 this business, having simply sold, acted as a sales agent for
17 Global, it had a duty to follow up and make sure that what
18 was going on was legitimate, and if it doesn't it could be on
19 the hook for everything that somebody else did, just to me
20 doesn't seem right, Your Honor.

21 And realistically when you're looking at actually how
22 these entities work, it wouldn't be possible for an
23 eight-person ISO to do that. It can't.

24 So then you say to yourself, well, I understand that
25 maybe practically speaking, but if the law says that, then

1 the law says that.

2 Well, I think we all can seek some solace in the fact
3 that the law doesn't actually say that. When you read the
4 statutes and you see the exceptions about people that are
5 processing things in the regular course and people that
6 knowingly recklessly provide substantial assistance, when you
7 see those standards you understand you don't fall into this
8 obligation by mistake.

9 You know, we're in a federal courthouse with the
10 government down from Washington for a company that went out
11 and had a merchant and submitted a sales application to
12 Global. And so you say, well, the cost, the expense to do
13 this -- and I submit to you, Your Honor, that *Apuzzo* was
14 decided in 2012. In 2010 was the Dodd-Frank Act. And in the
15 Dodd-Frank Act in the same spot where they had the
16 substantial assistance as it relates to the CFPA, they added
17 the substantial assistance in the security section. And in
18 our brief we at least argued that the concept of *in pari*
19 *materia* would say that if you have a standard that's in one
20 portion of the Act and you also have a standard in the other
21 portion of the Act, that those standards should be
22 interpreted the same.

23 And the Second Circuit case in *Apuzzo*, that standard has
24 been followed by other courts, as laid out in our brief, and
25 if the Court were to apply a different standard, then the

1 same language that was added in one section of the Dodd-Frank
2 Act would have a standard less or different than the standard
3 added in the other section of the Act.

4 And we submit to the Court that there's, looking at the
5 Act, there's no reason to believe that the Court would
6 deviate from the concept of *in pari materia* and treat those
7 two sections any different.

8 So then when you take a look and say, well, what does
9 Apuzzo say? Well, Apuzzo talks about aiding and abetting and
10 that's what the Act talks about, aiding and abetting, because
11 no one is contending that Pathfinder was actually calling
12 consumers or doing anything.

13 What it seems the CFPB is saying is that Pathfinder
14 should be on the hook for it.

15 Well, what does Apuzzo say? Apuzzo says that in order
16 to do that the defendant in some sort associated itself with
17 the venture, participated in it as something it wished to
18 bring about, and it sought by its action to make it succeed,
19 689 F.3d 204, Second Circuit, 2012.

20 Well, when you look at that standard and you've looked
21 at the concern that I suggested with the fact pattern, it
22 makes sense because if Pathfinder assisted the debt
23 collectors with the venture, participated in it as something
24 they wanted to bring about, and sought by its actions to make
25 it succeed, well, that would seem to make sense that if they

1 could allege that that maybe there should be some aiding and
2 abetting liability. But they can't allege that and they
3 didn't.

4 So you look at the standard that's in *Apuzzo* and say
5 that Pathfinder did not actually work with or in conjunction
6 with to make this happen. What happens in the arguments and
7 what happens in the briefing is that we then move to, well,
8 you shouldn't use *Apuzzo*, you should use a different
9 standard.

10 Well, I would note for the Court that in the CFPB's
11 opposition paper there is no discussion about *Apuzzo* with
12 respect to that definition. There is discussion about some
13 of the reckless language and whether the reckless language is
14 using a severe reckless and whether severe reckless was
15 before the Dodd-Frank Act, and then if Eleventh Circuit said
16 severe and then the Dodd-Frank said reckless, does that mean
17 it meant severe or didn't mean reckless?

18 But there's no argument in its opposition paper with
19 that definition that was determined by the Second Circuit as
20 it relates to substantial assistance. And we submit to the
21 Court that that is the appropriate standard and it's already
22 been determined and therefore Count VIII as it relates to
23 Pathfinder as pled cannot stand.

24 In addition, Count IX talks about unfair acts or
25 practices. Well, Pathfinder did not engage in any act or

1 practice in connection with any transaction with a consumer.
2 Pathfinder did not deal directly with the consumer.
3 Pathfinder didn't call a consumer. Pathfinder didn't sell
4 anything to a consumer. All Pathfinder did was send out an
5 independent sales agent to knock on the door of the flower
6 shop, get an application, return that application to Global,
7 and then Global entered into an agreement directly with the
8 merchant where -- in which it processed transactions that
9 were run with the merchant.

10 So by definition there was no consumer transaction, no
11 processing of payments, no offering of a consumer financial
12 product. And in addition, there's no aiding and abetting
13 liability for that particular section in Count IX. And we
14 included law in our paper that shows that if there's not
15 aiding and abetting liability in a particular statutory
16 section, that the United States Supreme Court said that the
17 Court can engraft that in there.

18 So the Count IX is kind of a collapse of two different
19 sections but the idea of the unfair practice doesn't have an
20 aiding and abetting piece.

21 So we submit to the Court that there's no unfair
22 practice by Pathfinder because it wasn't involved in any
23 consumer transactions.

24 In closing, Your Honor, I just submit that the Court, as
25 it noted at the beginning, has before it issues of first

1 impression. And in this case -- and the Court had asked a
2 question earlier at the beginning about why would we not wait
3 for summary judgment. Well, to us this is kind of the gate
4 issue and if the standard allows the gates to go past this
5 phase it will be crushing to eight-person companies to have
6 to go through the discovery in a federal court and go through
7 all that process.

8 And if the Court were to determine that the standard is
9 such that merely doing what Pathfinder did as described, or
10 as the CFPB may argue, is enough, then the punishment is
11 happening. The punishment is the process.

12 And in this instance, Your Honor, as it relates to the
13 question about summary judgment, Pathfinder already produced
14 over 21,000 pages of documents before we got here today and
15 submitted the depositions before we got here today. So the
16 CFPB had a whole host of information to plead a case, where a
17 lot of times the government doesn't have that kind of
18 information to plead, a lot of times most plaintiffs or
19 litigants don't have that kind of detail. But they had a
20 massive amount of discovery before they even filed in this
21 court.

22 So we'd submit to the Court that it's reasonable to
23 infer that whatever is in their complaint is what they've got
24 and I think that now is the time for the Court to decide
25 whether or not the standards are actually met by what was

1 pled.

2 THE COURT: Thank you.

3 MR. SMITH: Thank you.

4 MR. BALDRIDGE: Your Honor, can I just literally have 15
5 seconds so Mr. Engel can respond all at once?

6 THE COURT: If you can do it in 15 seconds --

7 MR. BALDRIDGE: I promise you.

8 THE COURT: -- but no more.

9 MR. BALDRIDGE: Number one, we don't get all the money.
10 The card brands are involved. I just want to take issue with
11 that comment that the majority of the money goes to us, just
12 so the Court doesn't have a misimpression.

13 Secondly, all we heard from both of them was who did
14 what, who does what. That's why you can't lump people
15 together as payment processors under Rule 9(b), because
16 there's vast disagreement over who did what and does what.
17 Thank you.

18 THE COURT: I'm not going to rule today so I'm going to
19 ask you to be brief because I've got folks who have been
20 waiting since 11:30 for their hearing that was set for 11:30.

21 MR. ENGEL: I understand, I'll try to tick off some
22 points, Your Honor.

23 That last one first with respect to the group pleading,
24 where we've alleged that payment processors -- and we've
25 identified that term -- where we've alleged that payment

1 processors did certain acts, we've alleged that each of those
2 payment processors has done that act.

3 Where we've used Frontline, Pathfinder, and Global and
4 alleged facts as to that particular entity, in that case only
5 that entity we've alleged engaged in the alleged conduct.

6 With respect to the sky-is-falling, doomsday scenario
7 and how could we possibly have known what was going on here,
8 I'd like to point out, and I'll stick to the pleadings here,
9 paragraph 180 of the complaint which identifies a specific
10 instance that resulted in this MATCH alert where another
11 payment processor identified that Universal was engaging --
12 after their own investigation -- that they were engaging in
13 factoring in excessive chargebacks and that payment processor
14 terminated these merchants. So I would point that out to the
15 Court for the point that it is in fact possible for them to
16 follow the policies and procedures to good effect.

17 And finally, I just want to address I guess generally a
18 causation question. With respect to substantial assistance,
19 the courts, at least as best as I can recall, are consistent
20 and I know that *Apuzzo* and *Subaye* are consistent in finding
21 that for a substantial assistance claim proximate cause is
22 not required and the primary violators' foreseeable acts are
23 not superseding causes of fraud.

24 And I'll add to that as briefly as I can that numerous
25 courts, in addressing consumer protection law under the FTC

1 Act, have found the conduct similar to that we've alleged
2 here has caused consumer harm.

3 And I'll end with a quote that: "One who places in the
4 hands of another a means of consummating fraud is himself
5 guilty."

6 THE COURT: In terms of the standards, the argument was
7 made that their duties, the duties arise under a contract;
8 your argument would be that a duty also arises where?

9 MR. ENGEL: That's the source of those duties, Your
10 Honor. And we argue that those are not necessarily duties
11 that are owed to consumers but those duties establish a
12 standard of care.

13 THE COURT: Thank you.

14 MR. ENGEL: Thank you.

15 THE COURT: Anything further?

16 MS. KANSKI: No, Your Honor.

17 MR. BALDRIDGE: No, Your Honor.

18 MR. SMITH: No, Your Honor.

19 THE COURT: Thank you all very much. This has been
20 helpful to the Court and I appreciate your efforts of being
21 brief with those because I know you all could have said lots
22 more if given the opportunity. I will take these matters
23 understand advisement. We will be issuing an order after
24 we've studied it thoroughly. You won't get an order in the
25 next week because I do think these are complex issues and I

1 do recognize that we're addressing some new issues and we
2 want to make sure that we get it right. So we're going to
3 take the time we need to do that but we will be proceeding
4 with it. It will be on a front burner because I like to do
5 it, when I've had an argument like this, while it's still
6 fresh with me, so we will be proceeding with these issues.

7 Thank you all for being here. Those who traveled from
8 afar be safe going home.

9 (Proceedings concluded at 12:30 p.m.)

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C E R T I F I C A T E

UNITED STATES DISTRICT COURT:

NORTHERN DISTRICT OF GEORGIA:

I hereby certify that the foregoing pages, 1 through 65, are a true and correct copy of the proceedings in the case aforesaid.

This the 14th day of August, 2015.

/s/ Amanda Lohnaas

Amanda Lohnaas, CCR-B-580, RMR, CRR
Official Court Reporter
United States District Court